



1942

### General Business Conditions

**T**HE business news of the past month has been dominated on the one hand by the increasing concentration on the war effort and progress in production, and on the other by demands from all sides for still greater speed and effectiveness. There are two possible interpretations of the criticisms and charges and counter-charges which groups of the people are directing at each other and at Washington. One is that they are evidence of conflicting interests, animosities, and a spirit of disunity which impairs the national strength and efficiency. The other is that only through free criticism and plain speaking, which assails slackness in any quarter and brings the force of public opinion to bear against any group which fails to subordinate its interest to the prosecution of the war, can the production effort reach its highest effectiveness.

Democracies are efficient in proportion to the understanding of the people and their unity of purpose. Much of the current criticism reflects a growth of understanding of what the war effort requires. People are discovering that the things the country has been doing are not the things that now have to be done. Economic policies of recent years have been to a large extent outgrowths of the great depression. They have been designed to make and spread work, but nothing could impair the productive effort more than policies to make and spread work now. They have been designed to redistribute income, to widen social benefits, and to increase the purchasing power of special groups, but under war conditions these policies invite and facilitate inflation. They have been designed to reform abuses and alleged evils in the economic system, but in doing so they have repressed enterprise, and the country now needs desperately all the enterprise that can be mustered.

Public opinion has become aware of the inconsistencies of conducting a war under policies that were designed to overcome a depression. The mobilization of the country's strength for war is being worked out according

## Economic Conditions Governmental Finance United States Securities

New York, April, 1942

to the democratic process, through people speaking their minds. In the long run nothing will be more effective in overcoming slackness and forcing special groups to conform to the needs of the emergency.

It is true that where criticisms are governed by animosity and ignorance or disregard of true conditions they give rise to a spirit of disorganization, but the practical sense and patriotism of the people may be relied upon to keep this spirit in check. It must also be relied upon to compose honest differences of opinion, and get ahead with the war effort. Where differences occur someone must compromise or give way, and when the decision has been made the national policy is entitled to full support.

### The Farmer-Labor Vicious Circle

Elements in the population, who otherwise strongly support the war program, are insistent on preserving and even improving their economic position. They are holding to this policy in the face of sacrifices that other groups have to make, and in the face of the indisputable fact that the costs of the war in the long run must be borne by all, either now and directly, or later in post-war disorganization. Farm leaders and leaders of organized labor each take the view that their group must maintain "parity" with the other, each disregarding the truth that when one makes a gain a countermove by the other naturally follows. The farmers have a price goal set forth in the law. This goal is "parity", which is defined in such terms that it rises with every increase in prices of the things farmers buy, and therefore provides new arguments for political action to raise farm prices as industrial wages and prices rise. Within the past month the House of Representatives, over the President's protest, included a provision in the Agricultural Appropriations Bill forbidding the sale of government-owned farm commodities below parity prices, although these supplies are now needed and although current prices combined with government payments yield parity to the grower. The bill now goes to the Senate.

These demands are matched by those of the labor leaders. While having no "parity" defined in law, labor finds its strongest argument for increased wage rates in rising living costs, which move up with farm prices. Nor are labor leaders satisfied, any more than the farm leaders, with maintaining pre-war living standards, as measured in the purchasing power of wages. In this Letter last month a chart was presented showing that the "real wage" of individual workers in the manufacturing industries has improved on the average about 25 per cent since the outbreak of the war; but now these workers are demanding and receiving further increases in wage rates, on the argument that the real wage will fall again unless hourly rates are marked up to keep pace with the rise in living costs.

It should be plain that farmers and organized labor are following each other around a circle. In due course the worker's living costs catch up with his wage gains and the farmer's costs with his price gains. Neither can improve his relative position except temporarily at the expense of the other, and each would be as well off, and in the long run better, if a halt were called to both. In this should lie the basis for a settlement.

Meanwhile other groups of the population, numerically larger than the farmers and organized labor combined, are caught in the rising price spiral. In the main these groups are helpless by-standers. They are without defense except as they can be defended by the Government, which is responsible for the farm laws and which has the legislative power to lay down a wage policy as well as a price policy. The situation is disruptive of mutual faith and confidence, which are the basis of unity.

Non-defense activities and expenditures of the Government constitute another area in which special interests prevail too often over the requirements of the war effort. It is represented that many of the activities criticized aid the war program, but public opinion is obviously skeptical of their value and resentful of their continuation. Welfare agencies established during the depression to keep the youth of the country busy, and for similar purposes, now constitute an unnecessary and unjust addition to the burden which people are carrying.

People want the money spent for war to go for war. They want the war vigorously and effectively carried on, its costs distributed as fairly as possible, and the general welfare put ahead of special interests. They want a suspension of disputes, and no special favors to anyone,—capital, labor, farmers or social workers. It should be easier to put the common purpose above special interests in wartime than in peace.

## The Production Achievement

Criticisms of the production effort should not dispel recognition of the production achievement. When after Pearl Harbor it became clear that output of consumers' durable goods would virtually end for the duration, predictions of declines in production indexes and of severe unemployment, pending conversion to war work, were common. Some of the comment indicated that cities like Detroit would become practically distressed areas. However, the conversion has gone faster than most observers had believed possible, and the armament output is exceeding earlier expectations accordingly. A dozen major industries have suspended civilian production entirely or almost entirely. But "priorities unemployment" is reaching only about half the totals predicted. In Detroit at the end of February 357,000 workers were employed, 60,000 less than during the boom one year earlier. In the first half of March an additional 18,000 found work, and the climb hereafter will be steady.

The Federal Reserve Board's index of industrial production has advanced each month. In February the figure was 173 (1935-39 = 100) compared with 166 in November and 144 in February a year ago, and preliminary estimates point to a further rise in March. The gains in arms production are more than offsetting all declines. Moreover, the index probably understates arms output, which is measured in most categories by the man-hours of work, for output per man-hour has made sensational gains.

This is a remarkable achievement in view of the conversion problem. It could not have been accomplished if waste and inefficiency in the direction and execution of the production program were as great as uninformed gossip would have it, or without skill and devotion by both management and labor. That still greater achievements will be marked up in the months ahead is certain. Mr. Nelson has cited instances where, if all plants utilized their facilities as fully as the plants having the best records, production could be increased 25 to 45 per cent. If the possibilities are measured by comparing present hours of machinery use with the maximum of 168 hours per week, theoretical gains are even greater.

Most people will understand that such comparisons are useful only as supplying a standard and a goal, for production is not wholly a problem of working every machine every minute, but of having the right things in the right place at the right time. This coordination becomes a task of mounting complexity as the slack in productive capacity is taken up.

With all the representations that are made against permitting each industry to do its own planning, it may be asked with reason who can do it better? The automobile industry, in the speed of its conversion since passenger car

output was stopped, is an example of what may be accomplished in an industry where the units are few and large, and where overhead coordination is in the hands of experienced automobile people detached from Washington. Other industries might benefit from similar administration.

The cotton textile industry is one which could take over full responsibility for doing its job. The president of the Cotton Textile Institute, Dr. Claudius T. Murchison, has pointed out that the industry is not homogeneous, with every unit prepared to manufacture any or all products, but is an aggregate of many industries. Coordination and allocation could increase its efficiency. It has in the Institute an organization through which it could work together, and has asked for a chance to do so but without avail because, in Dr. Murchison's words, "the Department of Justice says no". Plainly this is no time to employ any but the most effective industrial methods; and the common sense of the people will expect the Government to adapt its policies to that end.

#### Proposals to Limit Profit to 6 Per Cent

The industries are again under attack for alleged excessive profits on war contracts. Although the charges made in the Vinson report of last January have been effectively refuted by the demonstration that the average profit in all the cases given in the report, after allowance for taxes, was below the normal rate of return of manufacturing companies on their peacetime sales, the charges persist. New proposals are under discussion, and one has passed the House, to establish on all armament contracts limitations on profits similar to those in effect on naval and shipbuilding contracts before the defense program started. These limitations were fixed by the old Vinson-Trammell Act, which was suspended by the excess profits tax bill approved October 9, 1940. This suspension was for good reasons, and because of higher taxes the arguments against such limitations are stronger now than before.

The new Vinson proposal is to limit the return on war contracts to 6 per cent. Interest on funded debt, income and excess profits taxes, and certain other elements of costs could not be charged to the contract. Mr. Randolph Paul, the Treasury tax spokesman, pointed out that if the new Treasury tax proposals become law, even a company having no funded debt and not subject to the excess profits tax would have to earn 13½ per cent on the contract cost before taxes, in order to retain 6 per cent after taxes. If limited to 6 per cent, many companies could retain less than 1 per cent. The Undersecretary of War, Mr. Patterson, said such a limitation would virtually drive small businesses from war production. He pointed out its inequity by stating that a return of 6 per cent on cost of sales would provide an inadequate

return on capital in cases where the turnover is slow, while a contractor who turned his investment fifteen to twenty times a year could make over 100 per cent on capital.

The most fundamental error in the proposal, however, is the belief that the Government does not get its money's worth if the contractor makes more than an average profit. In many instances the facts are exactly to the contrary. The contractor gets the better than average return because through his own efficiency and skilled management he keeps costs below the estimates. The automobile industry is a case in point. Mr. Kanzler, chief of the Automotive Branch of the War Production Board, has stated that improved methods introduced by the industry were cutting 20 per cent from original estimated prices of most items and that economies in some cases ran as high as 40 per cent. This is the benefit of giving work to men who know how to do it.

It is wholly incorrect to assume that the savings made through these cost reductions will accrue continuously to the manufacturers. In many cases they pass back to the Government under the terms of existing cost-plus-fixed-fee contracts. In others they are passed back by lower prices on subsequent contracts, or even by renegotiation of fixed-price contracts. If in neither of these ways, they are recaptured through the corporation and excess profits taxes. As shown in the article on corporate earnings appearing subsequently in this Letter, increases in taxes took 90 per cent of the increases in earnings of large corporations in 1941. This was before the new tax proposals.

It is in the public interest to ask how much further than that the Government can hope to restrict earnings, without so increasing the possibility of loss as to weaken the incentive to expand plant and take on more work and more risks. Granting that patriotism is the highest incentive to production, neither the war effort nor the welfare of society is served by causing the war work to be done at excessive risk.

Public opinion upon proposals to put such arbitrary limitations on profits is confused by many misconceptions. One is the belief that profits are retained by the owners of the industries solely for their own welfare. But, apart from the exceptional cases of offensive extravagance, this is far from a correct statement of the case. The capital in use in the country is a fund primarily devoted to the welfare of society, and employed in ways permanently beneficial to all members of the community. It is the fund which supports production, finances the new ideas which are constantly incubating, and provides the improvements that are constantly needed. The corporations are the mechanisms by which men are employed, new discoveries developed and, now, the war effort carried on.



Corporations can exist, and the capital fund be replenished, only as there are profits in production. During the war it is necessary to tax profits heavily, and it is a sound principle that the war should not be the occasion for enrichment. But it should be understood that limitations on profits and the heavy corporation taxes both constitute a diversion to current use of capital normally destined for the industrial fund. The community should beware of carrying the seizure through in a spirit of reckless confiscation, for the sacrifice is most largely at the expense of society as a whole.

### The Treasury's Tax Proposals

The Treasury's proposals for raising the huge additional amounts of revenue needed to finance the war have been before Congress a month, and discussion of them has been going forward before the House Ways and Means Committee, in the public press, and among the people generally. Because of the fog of controversy enveloping the subject and the danger of subordinating primary to secondary considerations, it is important, in weighing the Treasury's proposals, to try to reduce the problem to its simplest terms. What is the main objective in raising taxes? Does the program proposed conform to this objective?

The answer to the first question was given by Secretary Morgenthau in his statement before the House Ways and Means Committee on March 3, when he named the control of inflation as the first goal of the new revenue act. "Nothing in the economic field," he asserted, "can interfere with the war effort as much as an uncontrolled rise in prices."

Continuing, the Secretary referred to the importance of non-fiscal devices such as price control, rationing, regulation of consumer credit, and the like, and then went straight to the heart of the tax problem as follows: "We should, therefore, tax so as to withdraw the greatest volume of purchasing power at this time, when money incomes are high and the quantity of goods for civilian use is shrinking day by day because of the demands of our war effort."

Here is a clear and unequivocal statement of the proper objective of wartime taxation. It remains to examine the program advanced in the light of these stated principles.

### Proposed Sources of New Revenue

The following table summarizes the sources from which additional revenue is proposed:

|                                 |                 |
|---------------------------------|-----------------|
| Individual income .....         | \$3,200,000,000 |
| Corporation .....               | 3,060,000,000   |
| Estate, gift .....              | 330,000,000     |
| Excise .....                    | 1,340,000,000   |
| From plugging "loopholes" ..... | 680,000,000     |
| Approximate total .....         | 8,610,000,000   |
| Less conflicting taxes .....    | 1,000,000,000   |
| Net total increase .....        | \$7,610,000,000 |

Additional to the foregoing tax increases, the Treasury proposed an increase in social security taxes amounting to \$2 billions, to be derived from extending the social security coverage and increasing tax rates.

How does this program conform to the principles of "withdrawing the greatest possible volume of purchasing power" from the markets? To answer this question it is necessary first to determine where the bulk of the increased purchasing power is being created, and then see to what extent the new taxes apply at those points.

### Where the New Income Is

The answer to the question, where the new income is being created, appears in the next table based on Department of Commerce figures and showing the increase in national income last year by major income groups:

National Income by Distributive Shares, 1940 and 1941  
(In Billions of Dollars)

|   | 1940   | 1941   | Increase |
|---|--------|--------|----------|
| Total compensation of employees .....         | \$52.6 | \$64.7 | \$12.1   |
| Salaries and wages .....                      | 48.9   | 61.1   | 12.2     |
| Total supplements to salaries and wages ..... | 3.7    | 3.6    | -0.1     |
| Work-relief wages .....                       | 1.6    | 1.2    | -0.4     |
| Social Security contrib. of employers .....   | 1.3    | 1.6    | 0.3      |
| Other labor income .....                      | .7     | .8     | 0.1      |
| Net income of incorporated business .....     | 5.6    | 7.3    | 1.7      |
| Dividends to stockholders, net .....          | 4.3    | 4.6    | 0.3      |
| Business savings .....                        | 1.3    | 2.6    | 1.3      |
| Net income of unincorporated business .....   | 11.5   | 14.6   | 3.1      |
| Agriculture .....                             | 4.4    | 6.2    | 1.8      |
| Other .....                                   | 7.1    | 8.4    | 1.3      |
| Interest (net) .....                          | 5.2    | 5.3    | 0.1      |
| Net rents and royalties .....                 | 2.2    | 2.5    | 0.3      |
| Total national income .....                   | \$77.1 | \$94.5 | \$17.4   |

It will be seen that out of an aggregate increase in national income amounting to \$17.4 billions, salaries and wages constituted \$12.2 billions, or approximately 70 per cent. Trailing far behind this huge increase in salaries and wages came gains in business profits and in agricultural incomes, and still further in the rear gains in corporate dividends, interest, and net rents and royalties.

These figures point conclusively to where the principal threat of inflation lies. It is in the swelling industrial payrolls, the vast bulk of which undoubtedly accrues to workers in the low income brackets. Salaries of executives account for but a minor share of the total. While in ordinary times an increase in income of the low income groups would be welcomed as lifting the general standard of living, it is unfortunately true that when the increase in purchasing power comes at a time of decreasing supplies of consumer goods, as at present, it is capable of great harm unless recaptured by the Treasury or diverted into savings.

### Where New Taxes Would Fall

Comparison of these facts as to income distribution with the Treasury tax proposals reveals the weakness of the program as out-

lined. Though the situation calls definitely for a broadly based program designed to reach all the people, the actual taxes proposed will fall mainly on the corporation and medium and higher individual incomes, leaving relatively untouched the great body of consumer incomes where the flow of new purchasing power is the greatest.

This is clearly true of the \$330,000,000 asked from estate and gift taxes, and of the \$680,000,000 of "loophole" taxes to be derived mainly from compulsory joint returns and abolition of tax-exempt interest from outstanding and future issues of state and municipal securities.

It is true of the \$3 billions additional asked in corporation taxes. Such taxes would have but little anti-inflationary effect, both because most of the earnings increase is already being skimmed off by existing taxes and because, for most corporations other than those in defense lines, priorities are making it increasingly difficult to spend earnings.

It is true of a large share of the \$3.2 billions more asked for in individual income taxes. For while the tax rates have been sharply increased, the tax-free exemptions of \$750 for single persons, \$1,500 for married persons, and \$400 for each additional dependent remain unchanged. This means, according to figures presented to Congress by Randolph Paul of the Treasury staff, that giving effect to personal exemptions and other normal deductions no income tax would be paid by single persons with incomes of \$832 a year, married persons with \$1,644 a year, and married persons having one dependent with \$2,106 a year. While Mr. Paul did not carry the figures further, it may be calculated that married persons with two dependents and normal deductions for interest, miscellaneous taxes, etc. might have tax-free income ranging as high as \$2,500.

#### How Many Escape Taxes?

Just how large a section of the population would escape income tax under these conditions cannot be said with certainty, but evidently it would be important.

The National Resources Planning Board calculated that in 1935-36 about 32 per cent of all consumer units in the country (families and single individuals) had incomes of less than \$750 a year, 69 per cent had incomes of less than \$1,500, and 89 per cent had incomes of less than \$2,500. According to the same source, families and single individuals having incomes of less than \$2,500 in 1935-36 accounted for 62 per cent of all consumer income.

More recently the Office of Price Administration has estimated that during the year 1941 approximately 78 per cent of all consumer units had incomes of less than \$2,500, and that in 1942 this proportion will be around 75 per cent, the decline being caused by the general

stepping up of the income average. The proportion of national income represented by the groups below \$2,500 was estimated at 44.5 per cent in 1941 and at 39.6 per cent in 1942.

While estimates of income distribution must always be taken with reservations, the available figures show beyond doubt that a large majority of the consumer units of the country, accounting for a predominant share of all consumer purchases, are outside the scope of income taxes. Admittedly, the general rise in incomes is bringing more families and individuals into the taxable brackets, but even so the proportion of such additional income reached by taxes must remain relatively small after exemptions and deductions ranging up to \$2,500 for the average family.

Only in the case of social security and excise taxes do the Treasury proposals give promise of tapping significant amounts of new consumer purchasing power at the critical points; and even here qualifications must be made for the half of social security taxes borne by the employer, and for such excise taxes as levies on pipe line transportation, lubricating oil, telephone and telegraph, which fall mainly or wholly upon business or the better situated individual incomes. Whether the \$242,000,000 of additional gasoline taxes could be realized depends largely on what happens to motoring.

In short, recapitulation of the Treasury program clearly indicates that the major share of the net total new taxes of \$9½ billions, including social security, will fall upon business and that minority of the population that has been carrying the bulk of the tax load thus far. Such a program is more calculated to reduce saving than spending. That taxes bearing so lightly on mass consumption can be successful in "withdrawing the greatest amount of purchasing power" or in effectively checking the price rise which Mr. Morgenthau fears, must be seriously doubted.

#### The Sales Tax Question

The foregoing would seem to demonstrate the need for some form of tax which would have wider coverage, particularly in the lower income groups which are not reached by direct income taxes and where most of the new purchasing power is being generated. As the public has become more fully aware of the magnitude of the sums to be raised and has gained a clearer understanding of the role of fiscal policy in the control of inflation, there has been marked growth of sentiment for some form of general sales tax.

Treasury officials in statements to Congress expressed strong opposition to the general proposition of further lowering the tax base and to a general sales tax in particular—the latter on grounds that it falls on scarce and plentiful commodities and necessities and

luxuries alike; that it bears disproportionately on the low income groups; that it increases prices and leads to demands for higher wages; and, finally, that it is difficult to collect.

There is undoubtedly a great deal of truth in many of the objections raised against the sales tax. No tax, however, is perfect and it is possible to raise objections to any form of tax. The problem is not one of finding the ideal tax, but is rather one of weighing alternatives and of finding the right combination of taxes.

A practicable tax program should seek to raise taxes by different methods, because different taxes affect people in different ways. The individual income tax is most effective in reaching the higher incomes, but as the tax rate rises in the different brackets it tends more and more to reduce savings rather than spendings. The withholding tax, deducted at the source, is more effective in reaching incomes in the lower brackets, but is difficult to collect from large numbers of people not on regular payrolls, and, like the income tax, cuts across saving as well as spending.

The sales tax, on the other hand, is particularly effective in reaching people who spend the major portion of their income and, broadly applied, is the only practicable form of tax that would reach everyone. While it is true that of and by itself it would place a disproportionate burden on the low income groups, when taken in conjunction with the very high corporate and progressive individual income taxes, it does not appear to be unfair. In fact, its impact upon the taxpayer is in some ways less severe than income or payroll taxes in that it leaves him some choice as to how much he pays. For it is a tax on spending pure and simple whereas income and payroll taxes are taxes on savings also. And it is spending, of course, that needs to be reduced to avoid inflation.

#### The T.N.E.C. Report on "Who Pays the Taxes?"

In the discussion over the tax program, objection was offered to additional taxes on the low income groups on the ground that these groups are already bearing more than their proportionate share of total taxes, including "hidden taxes." Reference was made to a Treasury study indicating that a single person earning \$750 a year (the present lower limit on taxable income) paid 17.3 per cent of his income in open and hidden federal, state and local taxes of all kinds, and a married man with no dependents earning \$1,500 paid 16.7 per cent.

While further details as to this study were not given, it has been assumed to be predicated on Monograph 3 of the Temporary National Economic Committee report, "Who Pays the Taxes?" The purport of this document, which covered the fiscal year 1938-39, was that the burden of taxes was especially heavy in the

income groups below \$1,000, became lighter in the groups of \$1,000 to \$10,000, and only became sharply progressive in the income groups above \$10,000. The results of this study were summarized in the following table:

All Taxes as Percent of Consumer Income, 1938-39

| Income classes             | Total consumer income (in millions of dollars) | Taxes as Percentage of Income |               | Total |
|----------------------------|--|-------------------------------|---------------|-------|
|                            |  | Federal                       | State & Local |       |
| Under \$500 .....          | \$ 2,363                                       | 7.9                           | 14.0          | 21.9  |
| \$500 to \$1,000 .....     | 10,038   | 6.6                           | 11.4          | 18.0  |
| \$1,000 to \$1,500 .....   | 12,280   | 6.4                           | 10.9          | 17.3  |
| \$1,500 to \$2,000 .....   | 10,210   | 6.6                           | 11.2          | 17.8  |
| \$2,000 to \$3,000 .....   | 12,194   | 6.4                           | 11.1          | 17.5  |
| \$3,000 to \$5,000 .....   | 7,743  | 7.0                           | 10.6          | 17.6  |
| \$5,000 to \$10,000 .....  | 4,861  | 8.4                           | 9.5           | 17.9  |
| \$10,000 to \$15,000 ..... | 2,238  | 14.9                          | 10.6          | 25.5  |
| \$15,000 to \$20,000 ..... | 1,601  | 19.8                          | 11.9          | 31.7  |
| \$20,000 and over .....    | 6,333  | 27.2                          | 10.7          | 37.8  |
| Total .....                | \$69,861                                       | 9.2                           | 11.0          | 20.2  |

The conclusions of Monograph 3 have been widely quoted, and this is not the first suggestion that they have been influential in determining fiscal policy. The validity of these conclusions is obviously a matter of importance. Actually, analysis of the report reveals reasons for questioning these conclusions.

In the first place, the report is based on previous studies of income distribution by the National Resources Planning Board, which in turn were based on small samplings and have been criticized by some economists both on grounds of inadequacy of data and for other reasons.

Second, the methods used have involved a number of controversial assumptions. For example, the treatment of social security payments as taxes has been criticized on the ground that such payments are in reality a form of savings, like premiums for the purchase of life insurance annuities. Criticism has also been made of the assumption in the report that all business taxes (other than taxes on net income) are passed on to the consumer. Certainly this has not been true of all real estate taxes in recent years, when much of the burden has had to be absorbed by the landlord; nor has it been wholly true of the railroads and public utilities.

Third, there appear to have been certain serious statistical errors. As one example, in adjusting the National Resources Planning Board figures on income distribution for 1935-36 to 1938-39, allowance was made for the increase in total national income during the period, but apparently no allowance was made for the fact that in any general rise in the total national income there would naturally be an upward movement of many family units from one income level to another. This tends to overstate incomes in the higher groups and understate those in the lower groups, hence distorting the relation of taxes to income.



Fourthly, and most significant, is the appearance of a serious discrepancy in the income distribution pattern of the T.N.E.C. report for the fiscal year 1938-39 and that shown by the Treasury statistics of income now available for those years. This is shown by the following table, giving the T.N.E.C. figures and averages of the Treasury figures on incomes above \$5,000, for the two calendar years 1938 and 1939.

**Individual Income in 1938-39, by Income Classes  
Over \$5,000**

| Income<br>Classes<br>(\$000s) | (In Millions of Dollars)            |                       |  |   |
|-------------------------------|-------------------------------------|-----------------------|--|---|
|                               | TNEC<br>Total<br>Consumer<br>Income | TNEC<br>Net<br>Income | Treasury Dept. "Statistics of Inc."<br>Total<br>Income | Treasury Dept. "Statistics of Inc."<br>Total Plus<br>Tax-exempt<br>Income |
| 5 to 10 .....                 | \$4,861                             | \$3,013               | \$3,522  | \$3,546   |
| 10 to 15 .....                | 2,238                               | 1,148                 | 1,366  | 1,387   |
| 15 to 20 .....                | 1,601                               | 653                   | 788  | 803   |
| 20 and over .....             | 6,333                               | 2,572                 | 3,124  | 3,241   |

A comparison of the figures is given only for the groups above \$5,000 because of the fact that the Treasury statistics compiled from individual income tax returns include only a limited number of taxpayers in the lower income groups, and because of the more thorough auditing of the higher returns.

In comparing figures from the two sources, allowance must be made also for differences in concept and definition of "income". The Treasury figures of "net income" are after allowable deductions such as interest, taxes, contributions, and business losses. Even if all these allowable deductions, however, were added to the "net income" as reported, and if wholly tax-exempt income were also included, the gross income of the \$5,000 and above groups, as shown in the last column of the table, would still be far short of the income imputed to those groups in the T.N.E.C. study. These discrepancies would seem to support other evidence that the income in the higher brackets has been overstated and that income in the lower brackets has been understated. This, of course, would directly distort the percentages derived of taxes to incomes in the different classes.

Monograph 3 states "it is frankly admitted that this is an experimental approach that requires further refinement" (a qualification seldom mentioned by those quoting the figures), and goes on to say that "it is hoped that the 1940 Census of Population, in conjunction with a more detailed analysis of 1939 income tax returns, will permit more accurate statistics on the distribution of incomes than the one used in the present report."

The discrepancies indicated by the Treasury income statistics for 1938-39 that have since been issued point to the need for a resurvey of the whole subject of income distribution and tax burden in the light of the new figures now available.

### Earnings of Leading Companies in 1941

Annual shareholders' reports for 1941 have now been issued by a large majority of all the corporations which make public their financial statements. These reports reflect the rise of general industrial and trade activity to new high levels, as well as a substantial rise in operating revenues of the railroads and public utilities, but show extremely uneven changes among different industrial groups in the net income as compared with the year 1940.

A tabulation of the reports of 2,540 companies for which comparative figures are available shows combined net income, less deficits, of approximately \$5,243 millions after taxes in 1941, which compares with \$4,367 millions for the same companies in 1940 and represents an increase of 20 per cent. Aggregate capital and surplus of this group at the beginning of 1941 was \$56,910 millions, upon which the average return was 9.2 per cent, compared with a net worth of \$56,163 millions and a return of 7.8 per cent in 1940. The following condensed summary shows the changes by major divisions.

**Summary of Net Income after Taxes of Leading  
Corporations in 1940 and 1941  
(In Millions of Dollars)**

| No.   | Division          | Net Income |         | % Change<br>1940-41 | % Return |      |
|-------|-------------------|------------|---------|---------------------|----------|------|
|       |                   | 1940       | 1941    |                     | 1940     | 1941 |
| 1,420 | Manufacturing     | \$2,665    | \$3,216 | + 21                | 10.5     | 12.4 |
| 125   | Mining & quar.    | 100*       | 124*    | + 24                | 6.3      | 7.3  |
| 133   | Trade .....       | 201        | 225     | + 12                | 10.4     | 11.3 |
| 231   | Transportation    | 215        | 542     | +152                | 1.8      | 4.6  |
| 151   | Public utilities  | 640        | 609     | - 5                 | 7.1      | 6.7  |
| 110   | Service & constr. | 45         | 58      | + 30                | 7.0      | 8.8  |
| 370   | Finance .....     | 501        | 469     | - 6                 | 8.5      | 7.9  |
| 2,540 | Total .....       | \$4,367    | \$5,243 | + 20                | 7.8      | 9.2  |

\*Before certain charges.

Our more detailed summary, given on the following page, shows the net income and net worth by major industrial groups. As pointed out heretofore, the financial results of leading companies, whose securities are listed on the exchanges and which promptly issue public reports, give a useful indication of trends, but do not provide an accurate measure of earnings for industry as a whole. The latter may be found only in the official "Statistics of Income" which are compiled by the Treasury Department from the tax returns of all corporations in the United States and become available a year or more later.†

†The latest detailed report on "Statistics of Income" (Part II, Corporations) is for the year 1938. Preliminary figures issued last February for 1939 showed in that year 469,617 active corporations, of which 199,479, or about 42 per cent, reported net income, while the remaining 270,138, or 58 per cent, had net losses. Their combined net income, including tax-exempt interest as well as intercorporate dividends received, amounted to \$5,946 millions after taxes. The latter figure represented an average return of 4.3 per cent on the \$137,314 millions net worth at the beginning of the year.

## NET INCOME OF LEADING CORPORATIONS FOR THE YEARS 1940 AND 1941

Net Income is Shown after Depreciation, Interest, Taxes, and Other Charges and Reserves, but before Dividends.—Net Worth Includes Book Value of Outstanding Preferred and Common Stock and Surplus Account at Beginning of Each Year.

(In Thousands of Dollars)

| No.   | Industrial Groups               | Net Income<br>Years |           | Per<br>Cent<br>Change† | Net Worth<br>January 1 |            | Per Cent<br>Return |      |
|-------|---------------------------------|---------------------|-----------|------------------------|------------------------|------------|--------------------|------|
|       |                                 | 1940                | 1941      |                        | 1940                   | 1941       | 1940               | 1941 |
| 22    | Baking .....                    | \$ 23,624           | \$ 23,002 | - 2.6                  | \$ 309,221             | \$ 311,796 | 7.6                | 7.4  |
| 15    | Dairy products .....            | 26,823              | 29,284    | + 9.2                  | 292,105                | 286,795    | 9.2                | 10.2 |
| 15    | Meat packing .....              | 30,979              | 50,302    | +62.4                  | 560,884                | 570,878    | 5.5                | 8.8  |
| 21    | Sugar .....                     | 9,780               | 11,937    | +22.1                  | 199,760                | 209,361    | 4.9                | 5.7  |
| 59    | Misc. food products .....       | 95,485              | 103,464   | + 8.4                  | 858,380                | 866,246    | 11.1               | 11.9 |
| 132   | Total food products .....       | 186,691             | 217,989   | +16.8                  | 2,220,350              | 2,245,076  | 8.4                | 9.7  |
| 17    | Soft drinks .....               | 40,689              | 45,332    | +11.4                  | 117,531                | 127,684    | 34.6               | 35.5 |
| 28    | Brewing .....                   | 12,998              | 14,621    | +12.5                  | 92,776                 | 97,837     | 14.0               | 14.9 |
| 14    | Distilling .....                | 22,654              | 27,317    | +20.6                  | 194,570                | 202,269    | 11.6               | 13.5 |
| 59    | Total beverages .....           | 76,341              | 87,270    | +14.3                  | 404,877                | 427,790    | 18.9               | 20.4 |
| 25    | Tobacco products .....          | 101,826             | 91,200    | -10.4                  | 753,949                | 781,906    | 13.5               | 11.7 |
| 50    | Cotton goods .....              | 15,967              | 36,407    | + .....                | 292,698                | 301,146    | 5.5                | 12.1 |
| 16    | Silk and rayon .....            | 22,792              | 24,249    | + 6.4                  | 239,998                | 248,818    | 9.5                | 9.7  |
| 7     | Woolen goods .....              | 4,972               | 10,876    | + .....                | 85,118                 | 92,113     | 5.8                | 11.8 |
| 17    | Knitted goods .....             | 3,100               | 7,481     | + .....                | 62,281                 | 63,332     | 5.0                | 11.8 |
| 39    | Misc. textile products .....    | 28,835              | 35,644    | +23.6                  | 257,607                | 268,625    | 11.2               | 13.3 |
| 129   | Total textile products .....    | 75,666              | 114,657   | +51.5                  | 937,702                | 974,034    | 8.1                | 11.8 |
| 24    | Clothing and apparel .....      | 8,711               | 11,852    | +36.1                  | 102,676                | 104,399    | 8.5                | 11.4 |
| 7     | Leather tanning .....           | 872                 | 3,093     | + .....                | 28,717                 | 28,671     | 3.0                | 10.8 |
| 19    | Shoes, etc. ....                | 15,330              | 19,812    | +29.2                  | 189,271                | 188,888    | 8.1                | 10.5 |
| 26    | Total leather products .....    | 16,202              | 22,905    | +41.4                  | 217,988                | 217,559    | 7.4                | 10.5 |
| 22    | Rubber products .....           | 41,750              | 56,022    | +34.2                  | 475,338                | 493,259    | 8.8                | 11.4 |
| 21    | Lumber .....                    | 8,997               | 15,462    | +71.9                  | 90,286                 | 94,778     | 10.0               | 16.3 |
| 10    | Other wood products .....       | 7,935               | 8,845     | +11.5                  | 74,323                 | 80,393     | 10.7               | 11.0 |
| 31    | Total wood products .....       | 16,932              | 24,307    | +43.6                  | 164,609                | 175,171    | 10.3               | 13.9 |
| 72    | Paper products .....            | 76,355              | 87,074    | +14.0                  | 798,773                | 829,911    | 9.6                | 10.5 |
| 32    | Printing and publishing .....   | 16,401              | 16,759    | + 2.2                  | 196,119                | 196,736    | 8.4                | 8.5  |
| 43    | Chemicals—industrial, etc. .... | 218,357             | 233,163   | + 6.8                  | 1,654,893              | 1,710,173  | 13.2               | 13.6 |
| 26    | Drugs, soap, etc. ....          | 70,873              | 71,680    | + 1.1                  | 327,965                | 334,033    | 21.6               | 21.5 |
| 8     | Fertilizer .....                | 2,008               | 3,476     | +73.1                  | 81,906                 | 81,717     | 2.5                | 4.3  |
| 14    | Paint and varnish .....         | 17,745              | 22,061    | +24.3                  | 222,780                | 226,926    | 8.0                | 9.7  |
| 91    | Total chemical products .....   | 308,983             | 330,380   | + 6.9                  | 2,287,544              | 2,352,849  | 13.5               | 14.0 |
| 34    | Petroleum products .....        | 322,587             | 462,431   | +43.4                  | 4,667,876              | 4,655,316  | 6.9                | 9.9  |
| 29    | Cement, gypsum, etc. ....       | 23,377              | 26,775    | +14.5                  | 298,060                | 302,428    | 7.8                | 8.9  |
| 41    | Other stone, clay and glass..   | 57,005              | 65,455    | +14.8                  | 497,421                | 507,512    | 11.5               | 12.9 |
| 70    | Total stone, clay and glass.... | 80,382              | 92,230    | +14.7                  | 795,481                | 809,940    | 10.1               | 11.4 |
| 57    | Iron and steel .....            | 282,231             | 326,142   | +15.6                  | 3,314,157              | 3,381,599  | 8.5                | 9.6  |
| 12    | Agricultural implements .....   | 52,923              | 67,527    | +27.6                  | 620,338                | 635,116    | 8.5                | 10.6 |
| 42    | Building equipment .....        | 40,501              | 45,225    | +11.7                  | 385,687                | 387,429    | 10.5               | 11.7 |
| 60    | Electrical equipment .....      | 140,966             | 147,963   | + 5.0                  | 918,569                | 946,482    | 15.3               | 15.6 |
| 54    | Hardware and tools .....        | 45,965              | 56,407    | +22.7                  | 305,110                | 316,561    | 15.1               | 17.8 |
| 33    | Household equipment .....       | 16,459              | 20,710    | +25.8                  | 127,143                | 129,619    | 12.9               | 16.0 |
| 134   | Machinery .....                 | 96,146              | 134,793   | +40.2                  | 643,346                | 683,912    | 14.9               | 19.7 |
| 21    | Office equipment .....          | 31,670              | 44,664    | +41.0                  | 257,639                | 261,381    | 12.3               | 17.1 |
| 20    | Nonferrous metals .....         | 134,291             | 157,093   | +17.0                  | 1,492,960              | 1,521,118  | 9.0                | 10.3 |
| 60    | Misc. metal products .....      | 53,652              | 65,073    | +21.3                  | 472,185                | 474,168    | 11.4               | 13.7 |
| 493   | Total metal products .....      | 894,804             | 1,065,597 | +19.1                  | 8,537,134              | 8,737,385  | 10.5               | 12.2 |
| 25    | Automobiles .....               | 251,204             | 276,647   | +10.1                  | 1,456,187              | 1,508,100  | 17.3               | 18.3 |
| 56    | Auto equipment .....            | 52,314              | 62,462    | +19.4                  | 293,235                | 314,108    | 17.8               | 19.9 |
| 27    | Railway equipment .....         | 34,951              | 51,623    | +47.7                  | 472,038                | 493,250    | 7.4                | 10.5 |
| 34    | Aircraft and parts .....        | 55,118              | 90,691    | +64.5                  | 145,689                | 185,683    | 37.8               | 48.8 |
| 6     | Shipbuilding .....              | 11,801              | 14,301    | +21.2                  | 39,447                 | 47,708     | 29.9               | 30.0 |
| 148   | Total transportation equip. ..  | 405,388             | 495,724   | +22.3                  | 2,406,596              | 2,548,849  | 16.8               | 19.4 |
| 32    | Misc. manufacturing .....       | 35,559              | 39,565    | +11.3                  | 330,314                | 320,015    | 10.8               | 12.4 |
| 1,420 | Total manufacturing .....       | 2,664,578           | 3,215,962 | +20.7                  | 25,297,326             | 25,870,195 | 10.5               | 12.4 |
| 29    | Coal mining .....               | 11,658*             | 20,621*   | +76.9                  | 538,557                | 544,175    | 2.2                | 3.8  |
| 45    | Metal mining .....              | 63,668*             | 68,109*   | + 7.0                  | 687,338                | 693,140    | 9.3                | 9.8  |
| 44    | Oil and gas .....               | 11,971*             | 22,937*   | +91.6                  | 278,016                | 275,537    | 4.3                | 8.3  |
| 7     | Misc. mining, quarrying .....   | 12,987*             | 12,561*   | - 3.3                  | 84,283                 | 84,361     | 15.4               | 14.9 |
| 125   | Total mining, quarrying .....   | 100,284*            | 124,228*  | +23.9                  | 1,588,194              | 1,597,213  | 6.3                | 7.8  |
| 15    | Chain stores—food .....         | 18,174              | 20,516    | +12.9                  | 202,093                | 209,831    | 9.0                | 9.8  |
| 46    | Chain stores—other .....        | 87,057              | 97,192    | +11.6                  | 727,996                | 752,806    | 12.0               | 12.9 |
| 26    | Department stores .....         | 17,162              | 18,812    | + 9.6                  | 218,754                | 224,664    | 7.8                | 8.4  |
| 5     | Mall order .....                | 61,055              | 61,525    | + 0.8                  | 503,379                | 527,628    | 12.1               | 11.7 |
| 41    | Misc. and wholesale .....       | 17,839              | 26,792    | +50.2                  | 281,433                | 282,962    | 6.3                | 9.5  |
| 133   | Total trade .....               | 201,287             | 224,837   | +11.7                  | 1,933,655              | 1,997,891  | 10.4               | 11.3 |
| 127   | Class I railroads .....         | 188,851             | 501,651   | + .....                | 10,817,381             | 10,753,495 | 1.7                | 4.7  |
| 37    | Traction and bus .....          | D-493               | 4,257     | + .....                | 483,489                | 474,972    | .....              | 0.9  |
| 8     | Shipping .....                  | 6,203               | 9,690     | +56.2                  | 91,675                 | 88,972     | 6.8                | 10.9 |
| 13    | Air transport .....             | 4,703               | 3,904     | -17.0                  | 30,643                 | 47,660     | 15.3               | 8.2  |
| 46    | Misc. transportation(a) .....   | 16,019              | 22,108    | +38.0                  | 400,701                | 400,645    | 4.0                | 5.5  |
| 231   | Total transportation .....      | 215,283             | 541,610   | + .....                | 11,823,889             | 11,765,744 | 1.8                | 4.6  |



## NET INCOME OF LEADING CORPORATIONS FOR THE YEARS 1940 AND 1941—Continued

| No.   | Industrial Groups              | Net Income Years |             | Per Cent Change† | Net Worth January 1 |              | Per Cent Return |      |
|-------|--------------------------------|------------------|-------------|------------------|---------------------|--------------|-----------------|------|
|       |                                | 1940             | 1941        |                  | 1940                | 1941         | 1940            | 1941 |
| 115   | Electricity, gas, etc (b)..... | 413,584          | 397,881     | — 3.8            | 6,064,377           | 6,130,732    | 6.8             | 6.5  |
| 36    | Telephone and telegraph .....  | 226,648          | 210,714     | — 7.0            | 2,907,984           | 2,942,604    | 7.8             | 7.2  |
| 151   | Total public utilities .....   | 640,232          | 608,595     | — 4.9            | 8,972,361           | 9,073,336    | 7.1             | 6.7  |
| 22    | Amusements .....               | 28,453           | 37,096      | +30.4            | 371,390             | 389,860      | 7.7             | 9.5  |
| 45    | Restaurant and hotel .....     | D-487            | 1,070       | +                | 96,416              | 92,373       | .....           | 1.2  |
| 26    | Other business services .....  | 11,858           | 13,092      | +10.4            | 112,230             | 113,856      | 10.6            | 11.5 |
| 17    | Construction .....             | 4,864            | 6,876       | +41.4            | 58,164              | 61,565       | 8.4             | 11.2 |
| 110   | Total service & const. ....    | 44,688           | 58,134      | +30.1            | 638,200             | 657,654      | 7.0             | 8.8  |
| 97    | Commercial banks .....         | 224,921          | 218,807     | — 2.7            | 2,639,148           | 2,724,455    | 8.5             | 8.0  |
| 80    | Insurance companies(c) .....   | 125,809          | 92,785      | —26.2            | 1,135,545           | 1,132,163    | 11.1            | 8.2  |
| 104   | Investment companies(d) .....  | 89,890           | 92,436      | + 2.8            | 1,574,777           | 1,508,125    | 5.7             | 6.1  |
| 44    | Sales finance companies .....  | 61,243           | 65,350      | + 6.7            | 475,720             | 499,918      | 12.9            | 13.1 |
| 45    | Real estate companies .....    | D-747            | 82          | +                | 84,521              | 83,231       | .....           | 0.1  |
| 370   | Total finance .....            | 501,116          | 469,460     | — 6.3            | 5,909,711           | 5,947,892    | 8.5             | 7.9  |
| 2,540 | Grand total .....              | \$4,367,468      | \$5,242,826 | +20.0            | \$56,163,336        | \$56,909,925 | 7.8             | 9.2  |

† Increases or decreases of more than 100 per cent not computed. D-Deficit. \* Before certain charges. (a) Includes stockyards, docks, warehousing, pipe lines, etc. (b) Figures refer to shareholders only. Because of the large proportion of bonded indebtedness, actual return on the property investment is less than the above. (c) Fire and casualty. Figures represent underwriting gain, and net interest, dividends and rents earned. (d) Net income shown as reported, not including such profits or losses on investments sold as were carried directly to surplus or reserve, nor changes in market value of portfolios.

## Effects of 1941 Taxes

One of the most interesting features in the 1941 shareholders' reports of many well-known manufacturing companies, aside from the record volume of sales last year and the conversion of plants and equipment to the production of war materials, was the heavy cut into net income resulting from the unprecedented total of federal taxes. Of the manufacturing companies in our tabulation, no less than 112 reported more than \$5 millions each in federal taxes payable on 1941 income. These large companies together had income tax liability of \$2,119 millions in 1941, compared with \$751 millions in 1940 and \$290 millions in 1939. Their large expansion in sales from 1940 to 1941 gave an increase of \$1,515 millions in net income before taxes, but it is probably not realized generally that 90 per cent of this increase was taken by taxes.

The following table shows the heavy but uneven extent to which taxes absorbed the increase in income of large manufacturing companies in selected major industries last year:

## Manufacturing Corporations Reporting Income and Excess Profits Taxes of Over \$5,000,000 Payable on 1941 Incomes

(In Millions of Dollars)

| No. | Industrial Groups         | Net Income Before Taxes |                | Income & Excess Profits Taxes |                | % of Increased Income Taken by Taxes |
|-----|---------------------------|-------------------------|----------------|-------------------------------|----------------|--------------------------------------|
|     |                           | 1941                    | Change 1940-41 | 1941                          | Change 1940-41 |                                      |
| 10  | Food and beverage.....    | \$219                   | \$+ 55         | \$ 95                         | \$+ 51         | 93                                   |
| 3   | Tobacco products .....    | 118                     | + 15           | 53                            | + 24           | 160                                  |
| 3   | Rubber products .....     | 91                      | + 47           | 56                            | + 40           | 85                                   |
| 11  | Chemicals & drugs .....   | 448                     | +143           | 242                           | +137           | 96                                   |
| 6   | Petroleum products .....  | 130                     | + 75           | 56                            | + 30           | 40                                   |
| 6   | Stone, clay & glass ..... | 106                     | + 35           | 56                            | + 33           | 94                                   |
| 14  | Iron and steel .....      | 672                     | +326           | 392                           | +298           | 91                                   |
| 8   | Electrical equipment..... | 389                     | +174           | 265                           | +190           | 103                                  |
| 13  | Machinery .....           | 162                     | + 77           | 109                           | + 68           | 88                                   |
| 9   | Autos & equipment.....    | 663                     | +235           | 387                           | +219           | 98                                   |
| 6   | Aircraft & equipment..... | 176                     | +125           | 131                           | +106           | 85                                   |
| 17  | Other metal products..... | 370                     | +155           | 203                           | +136           | 88                                   |
| 6   | Misc. mfg. ....           | 122                     | + 53           | 69                            | + 46           | 87                                   |
| 112 | Total .....               | \$3,716                 | +1,515         | \$2,119                       | +1,368         | 90                                   |

These 112 large companies alone have more taxes payable on their 1941 income than the sum-total of federal income and excess profits taxes ever collected from all manufacturing corporations in the United States (now around \$6,000) in any one of the 24 years 1916-1939 for which Treasury figures are available.

## Lower Profit Margin on Sales

The tendency for profit margins in the principal lines of manufacturing and trade to become narrower last year, in contrast with the usual experience when volume of business has a substantial increase, is illustrated by the table on the next page which shows the 1941 sales and net income after taxes for those companies whose sales figures are now available.

This group includes 966 manufacturing companies whose 1941 sales aggregated \$34,344 millions, and whose net income amounted to \$2,241 millions and was at an average rate of 6.5 per cent on sales. This compares with an average rate of 7.5 per cent computed for a similar although not identical group of companies from sales figures available for 1940. Net income after taxes as reported includes income from investments and all other sources, and therefore is considerably larger than the net income derived from sales alone.

An examination of the table will reveal that in almost every group the percentage of net income to sales in 1941 was lower than that for similar companies in 1940, despite the large increases which occurred in sales. In the iron and steel group, where sales by leading companies increased by about 55 per cent, the margin of profit declined from 8.1 to 6.2 per cent. In the automobile group, with a sales increase of 39 per cent, the margin decreased from 8.2 to 6.6 per cent.

**Percentage of Net Income after Taxes to Sales of  
Leading Corporations in 1940 and 1941**

(In Thousands of Dollars)

| No.          | Manufacturing         | Sales<br>1941 | Net Income<br>1941* | % Net Inc.<br>to Sales |      |
|--------------|-----------------------|---------------|---------------------|------------------------|------|
|              |                       |               |                     | 1941                   | 1940 |
| 16           | Baking                | \$ 455,330    | \$ 20,990           | 4.6                    | 5.2  |
| 12           | Dairy products        | 1,001,237     | 28,806              | 2.9                    | 3.2  |
| 13           | Meat packing          | 2,961,137     | 36,640              | 1.2                    | 1.3  |
| 19           | Sugar                 | 129,517       | 11,102              | 8.6                    | 8.1  |
| 35           | Food prod.—misc.      | 761,057       | 53,476              | 7.0                    | 7.5  |
| 43           | Beverages             | 626,070       | 37,235              | 5.9                    | 6.2  |
| 16           | Tobacco products      | 1,147,264     | 80,066              | 7.0                    | 8.9  |
| 35           | Cotton goods          | 496,621       | 28,723              | 5.8                    | 3.7  |
| 45           | Textile prod.—other   | 826,649       | 55,245              | 6.7                    | 5.0  |
| 17           | Shoes, etc.           | 400,986       | 18,595              | 4.6                    | 5.1  |
| 18           | Rubber products       | 1,274,484     | 54,360              | 4.3                    | 4.7  |
| 21           | Wood products         | 282,867       | 19,945              | 7.1                    | 6.5  |
| 57           | Paper products        | 635,430       | 51,902              | 8.2                    | 7.4  |
| 30           | Chemicals             | 840,733       | 76,417              | 9.1                    | 9.6  |
| 19           | Drugs, soap, etc.     | 500,931       | 61,170              | 12.2                   | 12.8 |
| 10           | Paint & varnish       | 322,645       | 14,909              | 4.6                    | 5.2  |
| 27           | Petroleum products    | 1,843,403     | 185,263             | 10.1                   | 7.3  |
| 47           | Stone, clay and glass | 672,735       | 49,761              | 7.4                    | 8.8  |
| 42           | Iron and steel        | 4,998,437     | 308,563             | 6.2                    | 8.1  |
| 10           | Agricul. implem.      | 790,893       | 63,331              | 8.2                    | 8.9  |
| 27           | Bldg. equipment       | 542,395       | 31,656              | 5.8                    | 7.6  |
| 27           | Electrical equip.     | 1,812,128     | 124,131             | 6.9                    | 10.4 |
| 33           | Household equip.      | 227,637       | 15,231              | 6.7                    | 8.1  |
| 31           | Machinery             | 923,823       | 81,517              | 8.8                    | 9.8  |
| 14           | Office equipment      | 370,295       | 37,483              | 10.1                   | 10.1 |
| 13           | Nonferrous metals     | 668,554       | 82,244              | 12.3                   | 14.1 |
| 63           | Metal prod.—other     | 1,013,491     | 71,759              | 7.1                    | 8.4  |
| 22           | Automobiles           | 4,168,853     | 274,301             | 6.6                    | 8.2  |
| 36           | Auto equipment        | 779,221       | 48,353              | 5.6                    | 6.8  |
| 17           | Railway equipment     | 521,776       | 34,348              | 6.6                    | 8.6  |
| 29           | Aircraft and parts    | 1,213,558     | 89,598              | 7.4                    | 13.1 |
| 5            | Shipbuilding          | 292,191       | 13,703              | 4.7                    | 8.1  |
| 67           | Misc. mfg.            | 851,698       | 83,752              | 9.8                    | 7.2  |
| 966          | Total mfg.            | 34,344,096    | 2,240,571           | 6.5                    | 7.5  |
| <b>Trade</b> |                       |               |                     |                        |      |
| 12           | Chains—food           | 1,245,225     | 17,151              | 1.4                    | 1.4  |
| 41           | Chains—other          | 2,054,510     | 95,735              | 4.7                    | 5.0  |
| 24           | Department stores     | 469,253       | 17,814              | 3.8                    | 4.0  |
| 5            | Mail order            | 1,640,476     | 61,525              | 3.8                    | 4.7  |
| 25           | Misc. & wholesale     | 450,944       | 13,041              | 2.9                    | 2.7  |
| 107          | Total trade           | 5,860,408     | 205,266             | 3.5                    | 3.9  |
| 1,073        | Total mfg. & trade    | \$40,204,504  | \$2,445,837         | 6.1                    | 6.9  |

\*Net income, after taxes, includes income from investments and other sources as well as from sales.

In aircraft and parts, whose sales last year trebled, after doubling in the preceding year, the margin declined from 13.1 to 7.4 per cent. The same tendency is found down the line of the other groups with but a few exceptions, such as cotton mills, and petroleum refining.

In the trade groups, the food chains, with a sales increase of about 16 per cent, showed their usual narrow margin of net income to sales unchanged at 1.4 per cent. There were slight declines in the average margins, taking group totals, for the chains other than grocery, and for the department stores, despite gains in sales of 16 per cent and 11 per cent, respectively. The mail order houses, with sales up 26 per cent to the highest levels in their history, nevertheless had a decline in margin from 4.7 to 3.8 per cent. This was due not only to rising costs, but to the sharp increase in income and

excess profits taxes, which absorbed practically all of the increase in net income and last year were far in excess of that remaining after taxes.

### Transportation

Last year the national defense program and rapid expansion of general business activity were accompanied by a heavy increase in the demands for freight and passenger service, which the railroads handled with a despatch and efficiency never before approached in this or any other country. The close cooperation which has been developed between the railroads, shippers and government departments concerned has been an important element in the success with which the many unusual demands for transportation during the past year have been met.

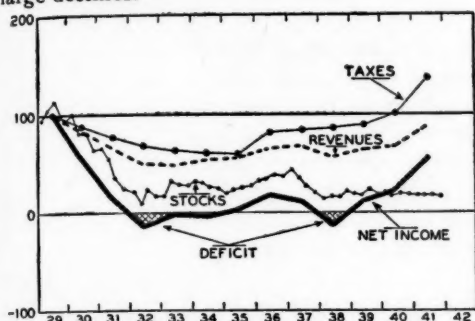
Total operating revenues for all class 1 railroads increased last year by 24 per cent, which permitted numerous companies to improve their financial condition materially, despite the substantial rise in operating expenses and taxes. Net income after interest charges and taxes more than doubled last year, reaching the highest point since 1930.

This sharp gain does not, of course, mean that the railroads and their shareholders have returned to a condition of prosperity following several years of lean earnings or deficits. The net income of approximately \$502 millions in 1941 represented an average return of but 4.7 per cent on the total corporate stock and surplus outstanding. Moreover, the portion of net income paid out in dividends to preferred and common shareholders represented a return on capital and surplus of but 1.7 per cent in 1941, compared with 1.5 per cent in 1940. Of the \$462 millions increase that took place in net income before taxes last year, \$149 millions was taken by taxes, \$297 millions was retained by the companies and applied toward reduction of debt or building up of assets, and only \$16 millions was added to the disbursements to shareholders who had provided the equity capital.

The limited dividend return on railroad stocks during the past several years, even in periods of heavy traffic and revenues such as are being experienced at present, together with a realization of the serious problems which the railroads will face during the next several years, probably go a long way toward explaining the prevailing depressed state of the share markets. The unusual variation between the movement of railroad stock prices and certain income and expense items for the period 1929-1941 are shown in the following chart, drawn from index numbers based on the 1929 average as 100.

It will be seen from the chart that, in terms of relatives based on the 1929 average as 100, the railroad operating revenues in 1941 stood

at 85, railroad taxes at 137, and net income at 56, while the index of railroad stocks closed the year at 16. Since the first of this year many high-grade railroad stocks have suffered further large declines.



All Class I Steam Railways in the U. S. Index Numbers, 1929=100. Computed from Statistics of Interstate Commerce Commission. Railroad Common Stock Prices from Standard & Poor's.

The long-term prospects of the railroads, including such questions as post-war readjustment and their relation to other transportation agencies, are matters which obviously must wait for the future to become even clearly defined. Immediate consideration, however, must be given to a number of important questions if the railroads are to continue to meet adequately the increasing traffic demands and at the same time work themselves back to a more healthy financial condition.

For example, how much further is the volume of railroad traffic likely to be increased by the stepping-up of war production and the diversion of more and more tonnage from the water and highway carriers? With existing railroad equipment generally being operated at near maximum capacity, and also subject to faster depreciation because of heavier loads, higher speeds and longer hours, what are the chances of the railroads to get large numbers of new cars and locomotives, plus maintenance and repair materials which they need and which in many cases have been on order for a long time?

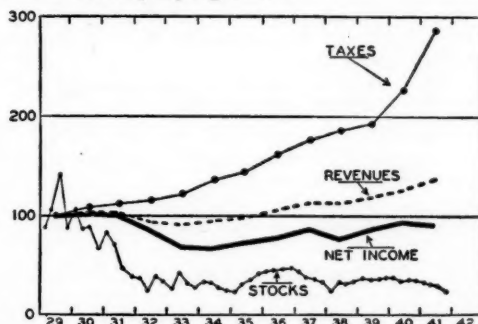
On the basis of 1941 traffic, the increase in freight and passenger rates recently granted will cover only 65 to 70 per cent of the wage increase; to what extent will the anticipated traffic increase of 10 to 15 per cent this year absorb the remaining costs? Allowance must of course be made also for higher tax rates; how will the railroads be affected by the proposed further increase in federal taxes, which have taken such a large portion of the recent increase in railroad income which otherwise might have been applied toward reduction of debt or paid to shareholders who have received little or no return for years? And will the new tax laws make any special provision for those railroads which have gone through reorganiza-

tion and as a result are now heavily penalized by the steep taxes on excess profits computed on their reduced capitalization?

Monthly reports of many systems for February 1942 show that traffic and operating revenues continued to run substantially ahead of the corresponding months of the preceding year, but that the rise in wages, taxes and supplies purchased more than absorbed the increase in revenues, causing net income to fall below that of last year. This reverses the upward trend that prevailed from 1938 through 1941.

#### Public Utilities

Representative public utility systems supplying electric, gas and other services reported an increase in operating revenues last year but a moderate decline in net income, due to the rise in taxes and operating expenses. The course of these items, together with a stock price index, for the period 1929-1941 is shown in the accompanying chart.



Electric Light and Power Industry in the U. S. Index Numbers, 1929=100. Computed from Statistics of Edison Electric Institute. Public Utility Common Stock Prices from Standard & Poor's.

From the standpoint of business volume, 1941 was the best year ever experienced by most utility systems. Measured by relatives based on the 1929 average as 100, the number of kilowatt hours sold in 1941 reached a new high of 186, at the same time that the average price charged per kilowatt hour for residential service reached a new low of 59. The financial results given on the chart show that in 1941 operating revenues established a new peak at 137, taxes soared to 287, net income declined to 90, and common stocks closed the year at 24.

The American Telephone & Telegraph Company and its 24 principal telephone subsidiaries had an increase of 11 per cent last year in operating revenues, but a decline of 9 per cent in net income, because of the rise in operating expenses and taxes. The latter reached a new peak of \$288 millions (excluding \$85 millions of taxes collected directly from customers), and represented 22c out of every dollar of revenues, nearly \$15 per share on the capital stock, or \$13 for every telephone in service.



# The BANKER *in* WARTIME

The banks of the United States have a major role in the war. They are the principal channel between the Treasury and the investor. They themselves are large buyers of government securities. They are a contact point between government and war industry. Their machinery is used at almost every step in the great war program. Fulfilment of this great responsibility will be aided by a clear definition and wide recognition of the banker's duties. That is the purpose of this statement.

## Financing the War

To avoid inflation the government must draw the funds it borrows primarily from the current income of individuals and institutions and only secondarily from commercial banks. It is the duty of the banks—

1. To encourage thrift and discourage spending so as to accumulate funds for war.
2. To push vigorously the sale of defense savings bonds and stamps and tax anticipation notes.
3. To subscribe for Treasury issues suitable for banks.
4. To help maintain a broad and dependable market for government securities.
5. To advise with the Treasury and the Federal Reserve System in planning government fiscal policies.

## Aid to War Production

Business large and small alike must be mobilized for war. The banker can help through his knowledge of business and government, and his ability to lend. It is his task—

1. To assist small business with war orders.
2. To finance war industry both in plant expansion and in current operations.
3. To participate with Federal financing agencies when the job extends beyond proper banking scope.
4. To advise with business customers in converting plants to war use, in dealing with government agencies, and in other war problems.
5. To lend to the farmer and distributor for the "Food for Freedom" defense program.
6. To scrutinize non-defense loans with care and to discourage expenditures which might compete with war production for materials or labor.
7. To cooperate in the regulation of consumer credit under Regulation W.



## Keeping the Economic Machine Running

The country's whole economic machine must be put in high gear to run as it never ran before. Almost every business transaction involves banking: the use of checks or money for buying materials or meeting payrolls, transferring funds, handling securities. The banker's ordinary job has become a war job. It is his responsibility therefore—

1. To provide for business and government deposit, checking transfer, and payroll facilities on a new, larger scale.
2. To sell and distribute vast numbers of defense bonds, stamps, tax anticipation notes, and handle tax checks.
3. To cooperate with the Treasury in dealing with foreign funds.
4. To offer special services for men in the armed forces.
5. To help interpret government to business and business to government that they may work together with understanding and unity.

These tasks must be carried through swiftly and accurately while many bank workers are entering military services. This means harder work for bank staffs from top to bottom.

## A House in Order

The nation faces years of great industrial and financial expansion and severe readjustments. To play his part effectively the banker's own house must be kept in order. It is his duty—

1. To maintain the quality of his bank's assets.
2. To husband his resources through a prudent policy of reserves and dividends.
3. To practice as well as preach the gospel of *work* and *save*.

## —and in the Community

As a citizen of his community the banker who is not himself called into the armed services has special obligations:

1. To share with others the responsibility for the success of the Red Cross, United Service and civilian defense.
2. To make local, state, and national bankers' organizations effective agencies in the nation's service.
3. To help the public understand war taxes, war restrictions, rationing, price controls, and other war measures which depend for their success upon public cooperation and public morale.

★ ★ ★

The National City Bank of New York endorses this statement which has been prepared by the Economic Policy Commission of the American Bankers Association

th g  
nash  
nate  
es. T  
nihil  
decia  
stam  
furn  
inen  
ertan  
ly wil  
a me  
span  
bank  
reac  
nd  
him  
s of  
nization  
tricia  
hich  
d pub